

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 4421-01
Bill No.: SB 573
Subject: Taxation and Revenue - Income, Veterans, National Guard
Type: Original
Date: January 17, 2018

Bill Summary: This proposal allows an income tax deduction for certain military personnel.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2025)
General Revenue*	\$0	\$0	(\$300,000 - \$700,000)	(\$2,800,000 - \$7,400,000)
Total Estimated Net Effect on General Revenue	\$0	\$0	(\$300,000 - \$700,000)	(\$2,800,000 - \$7,400,000)

* This proposal phases in 20% a year for five years.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2025)
Total Estimated Net Effect on <u>Other</u> State Funds	\$0	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses. This fiscal note contains 8 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2025)
Total Estimated Net Effect on All Federal Funds	\$0	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2025)
Total Estimated Net Effect on FTE	0	0	0	0

Estimated Net Effect (expenditures or reduced revenues) expected to exceed \$100,000 in any of the three fiscal years after implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS				
FUND AFFECTED	FY 2019	FY 2020	FY 2021	Fully Implemented (FY 2025)
Local Government	\$0	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Officials at the **Office of Administration Division of Budget and Planning (B&P)** assume this proposal would exempt National Guard and the reserve components of the Armed Forces from state income tax. The exemption would be phased in over 5 years, starting with tax year 2020, in 20% increments.

Due to data limitations, for the purpose of this fiscal note B&P will estimate a minimum and maximum loss amount for this fiscal note. B&P notes active duty pay was exempted under §143.174 for tax year 2016 and thereafter. Therefore, this proposal would only extend the income tax exemption to weekend pay for National Guard and other Armed Forces Reserve members.

Based on information from the Missouri National Guard, the average pay for Missouri National Guard soldiers totaled \$45.6 million in 2016, based on the average longevity of soldiers and excluding active duty and nonresident pay. B&P assumes that National Guard and other Armed Forces are paid similar salaries of approximately \$4,000 per year. In 2015, there were 7,820 Armed Forces reserve soldiers stationed in Missouri. Therefore, B&P estimates that Armed Forces reserves soldiers earned a total of \$30.5 million in Missouri during 2015. Based on the above information, B&P estimates that the total National Guard and Armed Forces Reserve minimum income was \$76.1 million. However, as noted above, the majority of this income is already exempt from Missouri income taxes. Therefore, B&P apportioned this annual income to the daily salary equivalent of \$2.0 million, by calculating the number of days the average National Guard and Armed Forces Reserves would typically work (38 days per year for the two weeks and two days per month). B&P then used these estimates to determine that total minimum weekend pay would be approximately \$48.1 million. Since income tax exemptions do not reduce Total State Revenue on a dollar for dollar basis, B&P estimates that this proposal will decrease Total State Revenue and General Revenue by a minimum of \$2.8 million once fully implemented.

Based on information published by the Missouri National Guard, the total average traditional pay for Missouri National Guard soldiers was \$118.6 million in 2016. B&P assumes that National Guard and other Armed Forces are paid similar salaries of approximately \$10,000 per year. In 2015, there were 7,820 Armed Forces reserve soldiers stationed in Missouri. Therefore, B&P estimates that Armed Forces reserves soldiers earned a total of \$79.5 million in Missouri during 2015. Based on the above information, B&P estimates that total National Guard and Armed Forces Reserve maximum income was \$198.1 million. However, as noted above, the majority of this income is already exempt from Missouri income taxes. Therefore, B&P

ASSUMPTION (continued)

apportioned this annual income to the daily salary equivalent of \$5.2 million, by calculating the number of days the average National Guard and Armed Forces Reserves would typically work (38 days per year for the two weeks and two days per month). B&P then used these estimates to determine that total maximum weekend pay would be approximately \$125.1 million. Since income tax exemptions do not reduce Total State Revenue on a dollar for dollar basis, B&P estimates that this proposal will decrease Total State Revenue and General Revenue by a maximum of \$7.4 million once fully implemented.

Table 1 shows the loss to Total State Revenue and General Revenue from this proposal by tax year.

Table 1: Impact by Tax Year

Tax Year	% Income Exempt	Loss to GR
TY20	20%	Greater than \$600,000 to Less than \$1,500,000
TY21	40%	Greater than \$1,100,000 to Less than \$3,000,000
TY22	60%	Greater than \$1,700,000 to Less than \$4,400,000
TY23	80%	Greater than \$2,300,000 to Less than \$5,900,000
TY24	100%	Greater than \$2,800,000 to Less than \$7,400,000

Table 2 shows the loss to Total State Revenue and General Revenue from this proposal by fiscal year.

Table 2: Impact by Fiscal Year

Fiscal Year	Loss to GR
FY20	Greater than \$300,000 to Less than \$700,000
FY21	Greater than \$900,000 to Less than \$2,200,000
FY22	Greater than \$1,400,000 to Less than \$3,700,000
FY23	Greater than \$2,000,000 to Less than \$5,200,000
FY24	Greater than \$2,600,000 to Less than \$6,600,000
FY25	Greater than \$2,800,000 to Less than \$7,400,000

Officials at the **Department of Revenue (DOR)** assume that beginning January 2020, the legislation allows a deduction for salaries or compensation from National Guard training or armed forces reserve components to the extent it was included in the federal adjusted gross income. The legislation allows for the deduction as follows:

ASSUMPTION (continued)

Beginning	Percent
January 1, 2020	20%
January 1, 2021	40%
January 1, 2022	60%
January 1, 2023	80%
January 1, 2024	100%

This may negatively impact General Revenue by an estimated \$2.8 million up to \$7.4 million when fully implemented in FY 2025. The range is due to the different data that was given to us by federal and state entities. The department notes that active duty pay was exempted under §143.174 for tax year 2016 and thereafter. Therefore, this proposal would only extend the income tax exemption to weekend pay for National Guard and other Armed Forces Reserve members. Since this proposed legislation does not begin until Tax Year 2020, the first Fiscal Year that would be effected is FY 2020.

Fiscal Year	Min. loss to GR	Max. loss to GR
FY20	0.3	0.7
FY21	0.9	2.2
FY22	1.4	3.7
FY23	2.0	5.2
FY24	2.6	6.6
FY25	2.8	7.4

Figures in \$M

The Department requires form changes and programming support to implement the provisions of this legislation. The Personal Tax Section requires one Temporary Tax Employee, one Revenue Processing Technician I for every 14,700 errors, and one Revenue Processing Technician I for every 5,700 pieces of correspondence generated.

DOR estimates the FTE costs at \$99,872 in FY 2019, \$100,345 in FY 2020 and \$101,156 in FY 2021. The Department assumes it will be able to absorb the above listed costs. If multiple bills pass which require Department resources and updates, the Department could request additional FTE's and related equipment and expenses through the appropriation process.

Officials at the **University of Missouri's Economic and Policy Analysis Research Center (EPARC)** assume this proposal would allow members of the National Guard and reserve components of the Armed Forces to deduct military income from their Missouri adjusted gross income.

ASSUMPTION (continued)

Although military income aggregates for Missouri are available from the Bureau of Economic Analysis, we are not able to discern between the incomes of active duty military and National Guard and reserve employees. As well, we are not able to identify employees of the National Guard or reserves within our simulation. Therefore, we are unable to provide an impact estimate of this bill.

Officials at the **Office of the Adjutant General** assume no fiscal impact to the Missouri National Guard.

Oversight notes this proposal creates a tax deduction that allows a person who receives salary or compensation to deduct that salary from their Missouri adjusted gross income. Those eligible for this deductions include those who are:

- 1) annual training status (AT) of the National Guard,
- 2) In performance of inactive duty for training (IDT) of the National Guard or; or
- 3) In reserve components of the Armed Forces of the United States.

Oversight notes that SB 814 adopted in 2016 created a tax deduction for active duty military members. It exempted 100% of the income received as a salary or compensation in any form as a member of the active duty component of the Armed Forces. Currently, DOR has interpreted SB 814 as exempting the income of those who receive the annual training status (AT) of the National Guard. Therefore, this proposal would not further impact them.

Oversight notes that SB 814 does not allow those who receive inactive duty training (IDT) to receive the 100% deduction. This proposal would expand this deduction to include them. This proposal would allow the phase in, 20% a year increasing to 100% in year five. Oversight asked the Missouri National Guard if they have any information on the number of people who participate in the inactive duty training over the last year. The estimated 9,127 people participated and received a combined salary of \$45,563,394.

Oversight notes that this proposal would be expanded to allow all members of the reserve components of the Armed Forces to claim the deduction. Oversight was unable to determine how many members of the reserve components of the Armed Forces reside in Missouri. The Missouri National Guard was also unable to estimate the number of reserves in Missouri. The Missouri National Guard told Oversight that approximately 9,200 Army and National Guardsmen live in Missouri.

ASSUMPTION (continued)

Oversight notes that the first deduction would begin with tax year January 1, 2020. Therefore, the first tax returns would be filed in FY 2021. Oversight for the fiscal note will show the impact as estimated by B&P and DOR, starting in FY 2021.

<u>FISCAL IMPACT - State Government</u>	FY 2019 (10 Mo.)	FY 2020	FY 2021	Fully Implemented (FY 2025)
GENERAL REVENUE				
<u>Revenue Reduction - deduction for military pay §143.175</u>	<u>\$0</u>	<u>\$0</u>	(\$300,000 to <u>\$700,000</u>)	(\$2,800,000 to <u>\$7,400,000</u>)
ESTIMATED NET EFFECT ON GENERAL REVENUE	<u>\$0</u>	<u>\$0</u>	(\$300,000 to <u>\$700,000</u>)	(\$2,800,000 to <u>\$7,400,000</u>)

<u>FISCAL IMPACT - Local Government</u>	FY 2019 (10 Mo.)	FY 2020	FY 2021	Fully Implemented (FY 2025)
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT - Small Business

No direct fiscal impact to small businesses would be expected as a result of this proposal.

FISCAL DESCRIPTION

This act allows members of the National Guard or reserve components of the Armed Forces of the United States to deduct such military income from his or her Missouri adjusted gross income to determine such taxpayer's Missouri taxable income. The percentage of such income that may be deducted shall be phased in between tax years 2020 and 2024 in twenty percent increments.

The income tax deduction authorized by this act shall apply to income received as salary or compensation in performance of Inactive Duty for Training (IDT) of the National Guard, Annual Training Status (AT) of the National Guard, or in reserve components of the Armed Forces of the United States. The deduction shall not apply to income received while engaging in civilian federal service, including civil service positions requiring the wearing of military uniform and military affiliation.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Department of Public Safety
Missouri National Guard
Department of Revenue
Office of Administration
Division of Budget and Planning
University of Missouri's Economic and Policy Analysis Research Center

Ross Strope



Acting Director
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